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July 23, 2007

Docket control  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, Arizona 85007

RE: Arizona Public Service Company's Initial Comments  
Competitive Procurement Workshop  
DOCKET NO. E-00000E-05-0431

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2007 JUL 23 P 4:49  
AZ CORP COMMISSION  
DOCKET CONTROL

Dear Madam or Sir:

Arizona Public Service Company is providing the attached comments in response to a request for written comments that emerged from discussions at the July 13, 2007 Competitive Procurement Workshop. APS appreciates the opportunity to work with Staff and the interested parties to address both resource planning and competitive procurement issues, and looks forward to on-going participation in these workshops.

If you have any questions or wish to discuss these matters further, please call me at 602-250-4563.

Sincerely,

*Barbara Klemstine / SC*

Barbara Klemstine

Attachment

BK/dtt

Cc: Ernest Johnson  
Barbara Keene  
Bing Young

Arizona Corporation Commission  
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**Arizona Public Service Company  
Competitive Procurement Practices  
Docket No. E-00000E-05-0431  
Second Set of Company Comments  
July 23, 2007**

The third and final Competitive Procurement Process workshop was held on July 13, 2007. At that workshop, the Staff of the Arizona Corporation Commission ("Commission") invited interested parties to provide written comments to address procurement procedures in general, as well as to specifically address the role and responsibilities of an Independent Monitor ("IM"). Arizona Public Service Company ("APS" or "Company") filed general comments regarding competitive procurement in this docket on May 25, 2007. The following comments address the specific issues discussed in the July 13<sup>th</sup> workshop.

### **Competitive Procurement Procedures**

APS believes that competitive procurement procedures should allow load-serving entities to efficiently and effectively examine market options in order to acquire adequate, reliable resources at reasonable costs. It is important to recognize that the competitive market is highly volatile and changes rapidly; therefore it is essential that a procurement process does not consist of requirements that would hinder the flexibility necessary for a utility to participate in the market when it is most advantageous. Undue delay or restrictions could preclude a utility from obtaining the most beneficial power procurement, which in turn could have a detrimental impact on its customers.

While the workshops on competitive procurement have discussed procurement in general, the specific focus has been on the appropriate procedures for formal solicitations, such as Request for Proposals ("RFPs"). Similarly, based on the discussions of the participants at the workshops, it appears that the interest in the use of an independent monitor is within the bounds of formal RFPs. APS believes this was an appropriate focus, and that the acceptable guidelines already exist, at least for APS, in relation to other long-term power procurement. There was also discussion as to whether the Track B protocols were an appropriate starting point for drafting new rules or guidelines. APS believes that the Track B protocols were appropriate in 2003 when Arizona had minimal experience with successful power solicitations, there was an overabundance of generation competing in the market place, and utility affiliates that developed generation were in existence. Since that time, Arizona utilities have successfully procured thousands of megawatts of long-term power through open solicitations, and the Commission has approved procurement protocols within the APS Code of Conduct.

A critical element of a competitive procurement process is that the formal competitive solicitation process, or RFP, must be conducted with integrity. The Company believes that formal protocols can provide some assurance that the utility is conducting its RFPs consistently and in a manner that is fair to the market. These protocols would be utilized for formal RFPs soliciting products with terms of five years or more, where there are no other specific protocols already in place (such as procurement under the Renewable Energy Standard Rules<sup>1</sup>). To that end, the Company is providing its recommendations for RFP protocols, which are attached as Exhibit A. In addition, APS already has in place a Code of Conduct

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<sup>1</sup> A.A.C. R-14-2- 1801 *et seq.*

that was approved by the Commission in Decision No. 68741 (June 5, 2006), which would address those circumstances where APS were to consider an affiliate proposal.

## **Independent Monitor**

At the July 13<sup>th</sup> workshop, Commission Staff indicated that they would be recommending to the Commission that there be a requirement for an IM in the competitive procurement process, and indicated that they were seeking comments regarding under what circumstances a monitor should be required and the scope of the IM's responsibilities.

### Circumstances Under Which An IM Could Be Utilized

As the Company has discussed in its Initial Comments and at the Competitive Procurement workshops, APS does not believe that an IM is essential for a cost effective competitive power procurement process where a utility affiliate is not participating as a potential seller. However, if the Commission determines that an IM may be desirable in other circumstances, the Company agrees with Staff that delineation of when the IM must be used should be clearly defined. If the Commission believes that an IM should have a role in a competitive procurement process, the Company believes an IM could be utilized in those circumstances where a utility is doing a **formal solicitation through an RFP for long term procurement for power or electrical generation**. A long-term procurement would be those seeking resources for a period of **five years or longer**.<sup>2</sup> Focusing the scope on formal solicitation for resources with terms of five years or more addresses the concerns of the interested parties, and avoids inappropriately encumbering the procurement of fuel, transmission, and short-term power as well as bilateral discussions. Under this approach, an IM would have been utilized in the six RFPs that the Company has issued over the past few years.

### The Role of the IM

APS believes the role of the IM should be to monitor the activities of all parties and evaluate a utility's procurement process in order to ensure that they adhere to fair and unbiased procurement practices. The Company believes that an IM's involvement with the procurement process should begin with the receipt of bids responding to an RFP. The IM should not perform independent economic, financial, or risk analysis; rather, the IM should examine the utility's efforts throughout the process, including a review of the Company's assumptions and analytics. While an IM should have access to appropriate Company personnel and pertinent data, it is unnecessary for an IM to be physically present during the term of the solicitation and selection process. The IM should be required to evaluate the process pursuant to the express standards specifically articulated by the Commission in formal policy statements, decisions or rules. The Company's proposed IM protocols are attached as Exhibit B.

### IM Selection

The Company believes that an IM must be independent of the utility and potential bidders, must be experienced and competent to perform all the IM functions, and must be recognized by the Commission as such. To avoid the potential for disputes regarding the competency and integrity of an IM, APS recommends that the Commission Staff and the utility both participate in the selection of an IM. The

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<sup>2</sup> The Settlement Agreement that was adopted by the Commission is Decision No. 67744 (April 7, 2005) defined long-term resources as five years or longer. See, Attachment A, paragraph 78(a).

utility and the Staff can each develop a "short-list" of acceptable IMs; and then jointly interview and select an IM.<sup>3</sup> To facilitate a timely and effective RFP process, the utility and Staff could work together to have the IM selected thirty days prior to the expected bid receipt date.

#### Recovery of Costs Related to the IM

Clearly, if the Commission directs the utility companies to engage a third-party IM to monitor the solicitation process, those related expenses are the cost of doing business and must be recovered by the utility (assuming the utility is charged by the Commission to pay for the IM). The Company believes that the most reasonable approach would be to recover those costs through bidders' fees. Bidders' fees serve two primary purposes: they provide an incentive to ensure that only entities that are serious about submitting a bid will respond to an RFP; and they assist in providing cost recovery for the time and resources it takes the utility to conduct the procurement process. This would include consultants or outside services that the Company may retain to evaluate issues related to the solicitation, as well as the cost of the IM.

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<sup>3</sup> A similar approach was utilized by Staff and the Company when APS was ordered to work with Staff to engage a consultant for a benchmarking study. Decision No. 68685 (May 5, 2006).

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**Guidelines for the Use of RFPs in the Long-Term**  
**Competitive Procurement Protocols**

The Company's proposed guidelines for the use of RFPs in long-term competitive procurement is intended to provide a framework for utilities to engage market participants in formal public solicitations or Request for Proposals (RFP) for electric power with terms of 5 years or greater. The goal is to establish a fair and equitable procurement process for the utility to seek to secure adequate and reasonably-priced long-term generation resources from the competitive electric market to meet the utility's future energy requirements. To be open, effective and successful, the solicitation process should do the following:

- (1) Engage market participants – The utility should provide public notice of its solicitation and may directly notify known interested market participants.
- (2) Identify acceptable products – Technologies, delivery requirements, operational performance requirements, terms, or other product requirements should be identified.
- (3) Identify the schedule – The timeframe for bid submittal evaluation, bidders' conference and selection should be provided to all potential respondents.
- (4) Outline the selection process – The utility should provide a description of the qualitative and quantitative factors it will consider in evaluating proposals and arriving at its final selection. Details on the analysis may not be provided publicly to protect confidentiality. Considerations related to any regulatory requirements or approval process should be identified.
- (5) Specify communications protocols – The utility should identify how information is to be communicated in order to provide adequate information exchange and avoid inappropriate treatment. This should include appropriate protection of confidential information.

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**Arizona Public Service Company**  
**Proposed Independent Monitor (IM) Protocols**

- **IM Scope of Work** would generally include monitoring the Request for Proposal (“RFP”) process, and the evaluation and selection process, as well as communicating with the Utility, Commission Staff and the Residential Utility Consumer Office (“RUCO”).
- In addition to determining whether or not the Utility complied with appropriate RFP procedures, the IM will determine if the solicitation was conducted in a fair, objective and impartial manner.
  - In monitoring the evaluation and selection of a proposal, the IM will:
    - Confirm that response data was appropriately applied;
    - Audit the evaluation process and validate the evaluation criteria, methods and models; and
    - Assure that the Utility used a fair and equitable process and made a reasonable selection.
  - Key communication protocols:
    - IM would immediately inform Utility of any issues so that the situation can be remedied.
    - IM would provide periodic status reports to Staff and the Utility regarding the solicitation process.
    - IM would submit a final report that addresses the IM’s observations, conclusions and recommendations regarding the RFP process to the Staff, RUCO and the Utility within two weeks of the final selection. Both a confidential version and a version that can be provided to the public must be submitted.
    - Any communication with the Utility or the respondents should be directed through the Utility’s designated point of contact.
    - The IM will be copied on all written and electronic communication between the Utility and the respondents.

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- All final documents prepared by the Utility will be provided to the IM in a timely manner.
- IM should be prepared to testify to their work at any regulatory proceeding relating to the solicitation.